No. 14,719

IN THE

United States Court of Appeals

For the Ninth Circuit

AUSTIN J. SHELTON,

Appellant,

vs.

GUAM SERVICE GAMES, a co-partnership,

Appellee.

APPELLEE'S REPLY BRIEF.

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APPELLEE'S REPLY BRIEF.

This case was tried in the Court below upon a written stipulation as to the operative facts. Accordingly, all of the facts are before this Court and no useful purpose would be served in reiterating those matters set forth in appellant's opening brief. We pass, then, to the sole issue involved.

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1. THE ISSUE.

The sole issue is whether a contract in question under the terms of which appellant agreed that he would not for a period of five years within the Territory of Guam engage in the coin operated machine

business in any manner or form either as owner, partner, agent, employee, or otherwise except as an employee of appellee is not restraint of trade. It should be noted that appellee purchased the coin operated machine business from appellant together with the good will thereof for the sum of $50,000.00.

Reference is made in appellant's opening brief to the applicable Guam law, to wit, Sections 1673 and 1674 of the Civil Code of Guam. As noted in the brief of appellant and in the opinion of the Honorable Court below, the principal difficulty arises from the interpretation of Section 1674. That section reads:

> "1674. *Exception, sale of good will.* One who sells the good will of a business may agree with the buyer to refrain from carrying on a similar business within a specified district, city or part thereof, so long as the buyer or any person deriving title to the good will from him carries on a like business therein."

Nowhere in the Civil Code of Guam is there a definition of the word "district."

The problem presented to this Court, then, resolves itself to a determination of whether an agreement to refrain from competing in the entire Territory of Guam is violative of Sections 1673 and 1674 of the Civil Code of Guam.

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2. THE RULE AT COMMON LAW.

In some cases the Court has expressed the view that, at common law, an agreement to refrain from engag-

ing in a similar business within an entire state or county is void as an unreasonable restraint of trade. However, this is not the true common law rule. The rule at common law is that the restraint may not be any greater than is reasonably necessary to protect the buyer of the good will of the business. The territorial limits of such restraint, will thus vary with the circumstances of the case. For example in *Nordenfelt v. Maxim-Nordenfelt Co.,* 1894 A. C. 535, a restraint from competing in a similar business for the entire world was held not to be unreasonable in view of the particular circumstances of the case.

The common law rule is well stated by the Court in *Wright v. Ryder,* 36 Cal. 342, decided before the present California Code sections with respect to the restraint in trade were enacted. The Court said at page 357 of the opinion:

> "The general principles which govern contracts in restraint of trade are well settled, both in England and the United States. They proceed on the theory that the public welfare demands that private citizens should not be allowed, even by their own voluntary contracts, to restrain themselves unreasonably from the prosecution of trades, callings, or professions, or from embarking in business enterprises in the promotion and encouragement of which the public has an interest. At an early period in English jurisprudence, when trade and the mechanic arts were in their infancy, it was deemed a matter of the greatest public importance to encourage their growth and to prohibit contracts which tended to abridge them. Hence the rule first established was, that

all contracts were void which in any degree tended to the restraint of trade, even in a particular, circumscribed locality, either for a definite or unlimited period. But as population and trade increased, and there was consequently a greater competition in all useful pursuits, the necessity for the stringent rule which before prevailed had in a greater measure ceased, and the rule itself was greatly relaxed and modified. Instead of denouncing as void all contracts in restraint of trade, the rule, as relaxed, tolerated such as were restricted in their operations within reasonable limits. Hence it has been repeatedly decided both in England and America, that whilst a contract by an artisan not to follow his calling at any time or place was an unreasonable restraint upon trade, contrary to public policy, and therefore void, nevertheless if he contracted for a valuable consideration not to pursue his occupation within certain reasonable, restricted limits, the contract was valid and would be enforced. Thus, in *Alger v. Thacher,* 19 Pick. 51, the defendant had entered into a bond by which he bound himself not to carry on the business of an iron founder at any time or place, and the Court held the contract to be void, as an unreasonable restraint upon trade. This is a leading case on that point. So, in *Keeler v. Taylor,* 53 Penn. 468, 469, the Court says: 'But if the restraint be general, that is, not limited to a reasonable time and district, it is void at law, and of course will not be enforced in equity.' In Story on Contracts, Sec. 550 the rule is thus stated: 'An agreement in *general* or *total* restraint of trade is void, although it be founded on a legal and valuable consideration. * * * The same rule has been uniformly adhered to even to

the present day; an agreement, therefore, not to carry on a certain business anywhere is invalid, whether it be by parol or specialty, or whether it be for a limited or for an unlimited time;' and he quotes in support of the rule *Mitchell v. Reynolds,* 1 P. Will. 190; *Homer v. Ashford,* 3 Bing. 323; *Pierce v. Fuller,* 8 Mass. 223; *Nobles v. Bates,* 7 Cow. 307; *Morris v. Coleman,* 18 Ves. 436; *Hinde v. Gray,* 1 Man. & Grang. 195; *Alger v. Thacher,* 19 Pick. 51; to which may be added many other authorities from the Courts of England and America. 'But,' he adds (Sec. 551), 'an agreement in *partial* restraint of trade, restricting it within certain reasonable limits or times, or confining it to particular persons, would, if founded upon a good and valuable consideration, be valid. * * * Such an agreement not only does not obstruct trade, but is oftentimes requisite and necessary, as well for the advantage of the public as of the individual.' This proposition is maintained in *Rannie v. Irvine,* 7 Mann. & Grang. 976; *Chappel v. Brockway,* 21 Wend. 157; *Hartley v. Cummings,* 5 C. B. 247; *Bunn v. Guy,* 4 East. 190; *Pierre v. Woodward,* 6 Pick. 206; *Perkins v. Lyman,* 9 Mass. 522; *Hayward v. Young,* 2 Chit. 407; *Mallan v. May,* 11 Mees. & Wels. 653; *Wickins v. Evans,* 3 Young & Jerv. 318.''

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3. THE FACTS HERE INVOLVED.

The restraint here is for the entire Territory of Guam. In determining whether such restraint is reasonable or unreasonable consideration must first be given to the area involved, the nature of the terrain

and the population. This Court may take judicial notice of the fact that Guam is an island approximately thirty miles in length with a maximum width of eight miles; that the northern one-third portion of the island is covered with a heavy rain forest, and the population according to the 1950 census is 59,498. We have thus a territory and a population comparable with a small California county. (The lower Court in its opinion fixes the area as about 225 square miles.)

The nature of the business involved and the price paid for it must also be taken into consideration. There is a popular phrase—"We're dealing in nickels and dimes." In this case we have a business where we don't even get to dimes. But the purchaser paid $50,000.00 for this business. Obviously in a business where the return is so small, where a number of persons available as potential customers is so few and where the price paid for the business is so large, a purchaser needs protection for his investment. As the Court said in *Great Western Distillery Products, Inc. v. John A. Wathen Distillery Company,* 10 Cal. 2d 442, 448, 449:

> "The decisions in this state have recognized and applied the distinction made by authority elsewhere that if the public welfare be not involved and the restraint upon one party be not greater than protection to the other requires, the contract will be sustained although it in some degree may be said to restrain trade. (*Associated Oil Co. v. Myers, supra,* p. 306; *D. Ghirardelli Co. v. Hunsicker,* 164 Cal. 355 [128 Pac. 1041]; *Grogan v. Chaffee,* 156 Cal. 611 [105 Pac. 745, 27 L. R. A.

(N.S.) 395]; *Herriman v. Menzies,* 115 Cal. 16 [44 Pac. 660, 46 Pac. 730, 56 Am. St. Rep. 81, 35 L. R. A. 318]; *Twomey v. Peoples' Ice Co.,* 66 Cal. 233 [5 Pac. 158]; *Schwalm v. Holmes,* 49 Cal. 665; *Noble v. Reid-Avery Co.,* 89 Cal. App. 75 [264 Pac. 341]; *Appalachian Coals, Inc. v. United States,* 288 U. S. 344, 360, 361 [53 Sup. Ct. 471, 77 L. Ed. 825]; *Board of Trade v. United States,* 246 U. S. 231, 238 [38 Sup. Ct. 242, 62 L. Ed. 683, Ann. Cas. 1918D, 1207]; *United States v. American Tobacco Co.,* 221 U. S. 106, 179, 180 [31 Sup. Ct. 632, 55 L. Ed. 663]; *Gibbs v. Baltimore Gas Co.,* 130 U. S. 396, 409 [9 Sup. Ct. 553, 32 L. Ed. 979]; *Peerless Pattern Co. v. Gauntlett Dry Goods Co.,* 171 Mich. 158 [136 N. W. 1113, 42 L. R. A. (N.S.) 843], and cases cited in note; *J. W. Ripy & Son v. Art Wall Paper Mills,* 41 Okl. 20 [136 Pac. 1080, 51 L. R. A. (N.S.) 33].)"

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4. THE PUBLIC POLICY INVOLVED.

Contracts in restraint of trade are not *per se* bad. A contract restraining one from following a lawful trade or calling may be invalid because it discourages trade and commerce, and prevents the party from earning a living, but the right to agree to refrain from his calling, within reasonable limits as to space may have the contrary effect. It encourages trade, for it gives value to a custom or business built up by making it salable. In considering these factors, the California Supreme Court said in *Brown v. Kling,* 101 Cal. 295, 300:

"One rule at common law applicable to this matter was that the restraint should be no greater than is necessary to protect the purchaser. * * *"

The California Supreme Court in *City Carpet, etc., Works v. Jones,* 102 Cal. 506, 511, involving a contract in which the seller of a business agreed to refrain from competition in the Counties of San Francisco, Alameda and San Mateo, said:

"At common law the territorial restriction imposed by this contract would doubtless have been considered valid, inasmuch as a portion of the value of the goodwill may have accrued from customers residing in these contiguous counties, though the business was conducted in one alone; and the purchaser, unless restricted by statute, or by a controlling public policy, was entitled to the whole of the goodwill which he purchased and paid for. It was not, therefore, at common law an illegal contract, nor are such contracts declared by the statute to be illegal. They are simply void so far or to the extent that they exceed the restrictions imposed by the statute. The code introduces no new principle; it simply eliminates from the controversy arising upon such restriction the question as to what is a reasonable territorial limit, by specifically defining it, and thus preventing litigation; and in this the statute is wise and salutary, even though in certain cases, possibly in this one, it gives the purchaser less than he bought and less than he might enjoy without violating the interests of the public. The statute imposes no penalty upon the purchaser under such contract, nor could it require the seller to resume business."

5. THE EFFECT OF THE GUAMANIAN CODE UPON THE COMMON LAW RULE.

As the Supreme Court of California pointed out in *City Carpets, etc., Works v. Jones,* 102 Cal. 506, 511 and reiterated in *Merchants Ad-Sign Co. v. Sterling,* 124 Cal. 429, 433:

> "* * * the code introduces no new principles; it simply eliminates from the controversy arising upon such restrictions the question as to what is a reasonable territorial limit."

With this in mind, we must look to the provisions of the Guamanian Code to see whether it is merely declarative of the common law or whether it substitutes a specific territorial limit to replace the uncertain rule of the common law which depends upon "reasonableness". It is significant that the stipulation of facts in this case states that the word "district" is of no territorial significance. The inclusion of the word "district" in the Guamanian Code is thus open to two constructions:

A. It is meaningless and the rule of the common law is applicable.

B. It is of some meaning territorially.

If we adopt proposition A as the proper premise, then the rule as to allowable restraint is the common law rule. If this be so, a restraint for the Territory of Guam, a small, sparsely populated island, is not an unreasonable restraint in the sale of a business and goodwill for the sum of $50,000.00.

If we adopt the second proposition, then we must look somewhere outside of the Guamanian Code for the meaning of the word "district". Black's Law Dictionary, Fourth Edition, page 562, gives the following definition:

> "*District.* One of the portions into which an entire state or country, county, municipality or other political subdivision or geographical territory is divided, for judicial, political, or administrative purposes. Briggs v. Stevens, 119 Or. 138, 248 P. 169; State ex rel. Schur v. Payne, 57 Nev. 286, 63 P.2d 921, 925.
>
> "The United States are divided into judicial districts, in each of which is established a district court. They are also divided into election districts, collection districts, etc.
>
> "The circuit or territory within which a person may be compelled to appear. Cowell. Circuit of authority; province. Enc. Lond."

We find—and the parties have so stipulated—no segregation of Guam as to geographical districts. However, there is a Judicial District of Guam. If the Judicial District is the district referred to in the Guamanian Code, it includes the entire Island of Guam, and thus the contract in question does not fall within the ban of the code section.

The attention of the Court is directed to the well established rule of statutory construction that when a contract is capable of two constructions, the one making it valid and the other void, the first ought to be accepted. See *Herzog v. Purdy,* 119 Cal. 99; *McVicker*

v. McKenzie, 136 Cal. 656, 660; *Pacific Wharf Co. v. Standard American Dredging Co.,* 184 Cal. 21, 25.

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6. REPLY TO APPELLANT'S CONTENTIONS.

Commencing with page 13 of his brief, appellant seeks for a strained construction of the word "district". He tells us that in applying the California Code to the Guamanian situation, the term "district" was substituted for the word "county". He tells us then that by reason thereof the Guamanian codifier must have meant a specific territorial limitation, but it nowhere appears what that specific limitation was. It is significant that in the division of Guam into a district for purposes of the jurisdiction of its only court, the Code encompasses the entire territory.

We have no quarrel with the definition of the word "district" as given in *Olive v. State,* 11 Neb. 1, 13-14, 7 N.W. 44; *Hammond v. Young, et al.,* 117 N. E. 2d 227, 231; *City of Louisville, M. H. Commission v. Public Housing Admin.,* 261 S. W. 2d 286 or the other cases cited by appellant. In fact these cases lend strength to our position. Particular attention is directed to the portions of the opinions in *Hammond v. Young* and *City of Louisville, M. H. Commission v. Public Housing Admin.* which appellant has cited in his brief.

CONCLUSION.

For the foregoing reasons, it is respectfully submitted that the judgment of the lower Court is correct; that the Guamanian Code either is merely declarative of the common law which imposes a "reasonable" territorial restriction or the word "district" as used in said Code must mean the only district of any territorial import that we have been able to find—the area over which the jurisdiction of the District Court of the District of Guam, Territory of Guam is exercised.

Dated, San Francisco, California,
November 1, 1955.

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